SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1922

No. 431

THE PUSEY AND JONES COMPANY
(a corporation)
Petitioner

against

HANS KARLUFF HANSSEN
Respondent

AND

JACOB PREBENSEN, JR., H. KJERSHOW, HARRY BORTHEN, A/S TROMP, A/S MARITIM, A/S HAUG, A/S MERCATOR, A/S SORLANDSKE LLOYD, and E. & N. CHR. EVENSEN
Intervenors-Respondents

Brief on Behalf of Petitioner

LINDLEY M. GARRISON
CHARLES H. TUTTLE
SELDEN BACON
SAUL S. MYERS
Counsel for Petitioner

Appeal Printing Company, 22 Thames Street, New York City

SUBJECT INDEX.

BRIEF OF THE ARGUMENT.

PAGE

STATEMENT OF THE CASE 1
History of Proceeding 3
The Intervenors 5
Principal Questions Presented 6
Specifications of Error 7

FIRST POINT.—Hanssen's claim is at best but that of an alleged simple contract creditor of the Pusey & Jones Company. His claim is disputed in its entirety and has not been reduced to judgment. He holds no lien upon the property of the company. The company made timely demand of a common law trial by jury of Hanssen's claim

Hence, the United States District Court sitting in equity should not have entertained his bill, and had no jurisdiction to do so under the statute of Delaware or otherwise 8
(1) Rule in courts of equity in the absence of State statutes 12
(2) Rule in the Federal Courts under state enabling statutes 13
(3) Decisions claimed to be contrary, distinguished 18

SECOND POINT.—The orders below rest on an interpretation of the Delaware Statute, which purports to enlarge the jurisdiction of the Federal Court in equity and to empower it to determine an ordiinary common law claim under the guise of merely

PAGE

supplying an auxiliary remedy in equity. That interpretation obliterates the line of demarcation in the Federal Courts between common law and equitable causes and deprives the defendant of its constitutional right to a jury trial under the Seventh Amendment to the United States Constitution 24

THIRD POINT.—The Delaware Statute has never been construed, except in the decisions below, as authorizing a simple contract claimant, whose claim is disputed by answer demanding a jury trial and who has no legal or equitable lien on the property of the corporation, to institute a creditor's bill under the statute 33

FOURTH POINT.—The Bill of Complaint prays for no final relief whatever with respect to Hanssen's alleged rights as a creditor. The Federal Court, therefore, was without jurisdiction to appoint Receivers for the assumed protection of his rights as a creditor; and any interpretation of the Delaware Statute which would authorize it to appoint Receivers on such a bill and for such a purpose would clearly work an enlargement of the jurisdiction of the Federal Court and hence not be permissible .. 37

FIFTH POINT.—As to Hanssen's claim to be a creditor, the only question now relevant is whether the courts below were right in holding that the issues involved in this claim must, over the defendant's protest, be tried by the Federal Court in Equity.

But, in any event, Hanssen clearly did not sustain the burden of proof that he was a creditor of the Company. The contrary appeared 12

PAGE

SIXTH POINT.—The plaintiff's alleged status as a stockholder has not been considered in the courts below to be, and is not, sufficient ground of jurisdiction. Consequently, the question as to his status as a stockholder is not here as a question of law for determination 53

SEVENTH POINT.—The Pusey & Jones Company was greatly aggrieved and irreparably damaged by the jurisdiction assumed and the decrees made below 59

CONCLUSION.—The decrees below should be reversed; the Bill of Complaint dismissed; and the Receivership vacated, with costs.. 60

TABLE OF CASES.

Adler *v.* Campeche Laguna Corporation, 257 Fed., 789 27
Adler *v.* Seaman, 266 Fed., 828 .....6, 41
Alderson *v.* Dole, 74 Fed., 29 41
American Can Co. *v.* Erie Preserving Co., 171 Fed., 540 13
Amsinck *v.* Rogers, 189 N. Y., 252 49
Atlanta & F. R. Co. *v.* Western Ry. Co., 50 Fed., 790 .....18, 29
Atlanta, etc., Co. *v.* Carolina Cement Co., 140 Ga., 650 6
Baldwin *v.* Canfield, 26 Minn., 43 58
Blake *v.* Langdon, 19 Vt., 485 53
Boston & M. R. R. *v.* Sullivan, 275 Fed., 890... 6
Brant, *In Re*, 96 Fed., 257 40
Brictson Mfg. Co. *v.* Close, 280 Fed., 297 40
Burns *v.* City of Atchison, 48 Kans., 507 41
Cates *v.* Allen, 149 U. S., 451 .....16, 19, 20, 22, 23
Clark *v.* National Linseed Co., 105 Fed., 787 .. 41
Closser *v.* Strawn, 227 Fed., 139 31
Creston National Bank *v.* Salmon, 117 Mo. App., 506 50
Continental Trust Co. *v.* Toledo, etc., R. Co., 82 Fed., 642 (aff'd 95 Fed., 497) 12, 23

PAGE

Cowley *v.* Northern Pacific Railroad Co., 159 U. S., 569 ..... 19, 22, 23
Czerney *v.* Haas, 141 App. Div., N. Y., 430 51
Darragh *v.* H. Wetter Mfg. Co., 78 Fed., 7 .18, 20, 21
Davidson *v.* Alfaro, 80 N. Y., 660 52
Davis *v.* Hayden, 238 Fed., 734 23
Davidson-Wesson Implement Co., Ltd., *v.* Parlin & Orendorff, 141 Fed., 37 17
De Rees *v.* Costaguta, 275 Fed., 172; appeal dismissed, 254 U. S., 166 40
Dubreuil *v.* Gaither, 98 Me., 541 53
Duplex Printing Press Co. *v.* Deering, 254 U. S., 113 32
Elyea *v.* Lehigh Salt Mining Co., 169 N. Y., 29 58
Garner *v.* Price, 4 Kulp., 10 53
Gillespie *v.* Riggs, 253 Fed., 943 ..... 13, 23
Gorman-Wright Co. *v.* Wright, 134 Fed., 364.. 58
Grand Chute *v.* Winegar, 15 Wall., 373 24
Gutterson & Gould *v.* Lebanon Iron & Steel Co., 151 Fed., 72 40
Harrison *et al.*, *v.* Farmers' Loan and Trust Company of New York, 94 Fed., 728 18
Hobbs *v.* Duff, 23 Cal., 596 53
Hollins *v.* Brierfield Coal and Iron Co., 150 U. S., 371 ..... 11, 12, 14, 15, 22, 23
Hovey *v.* Elliott, 167 U. S., 409 32
Hunter *v.* Fiss, 92 App. Div., N. Y., 164 51
Hutchinson *v.* American Palace Car Co., 104 Fed., 180 ..... 40, 41
Janness *v.* Bean, 10 N. H., 656 51
Jacobs *et al. v.* Mexican Sugar Co., 130 Fed., 589 ..... 18, 20
Jones *v.* Mutual Fidelity Co., 123 Fed., 506 ...20, 21
Leeds *v.* Marine Ins. Co., 6 Wheat., 565 53
Lindsey *v.* Jackson, 2 Paige, 581 53
Louisville & N. R. R. Co., *v.* Western Union Tel. Co., 234 U. S., 369 23
Matthews Slate Co. *v.* Matthews, 148 Fed., 190 ..... 18, 23, 28, 34
Maxwell *v.* McDaniels, 184 Fed., 311 13
McGraw *v.* Mott, 179 Fed., 646 22

PAGE
McLean *v.* Lafayette Bank, 16 Fed. Cas. No. 8887 40
Mesa Mellon Growers Asso. *v.* Byrnes, 211 Ill. App., 236 6
Metropolitan Ry. Receivership, 208 U. S., 90..21, 34
Mississippi Mills *v.* Cohn, 150 U. S., 202 ....14, 15
Moe *v.* Thomas McNally & Co., 138 App. Div., N. Y., 480 34
Morrow Shoe Mfg. Co. *v.* New England Shoe Co., 57 Fed., 685; aff'd. on rehearing, 60 Fed., 341 .....18, 29
Nesbit *v.* North Georgia Electric Co., 156 Fed., 979 13
Norris *v.* N. Y., N. H. & H. R. R. Co. (a decision by Circuit Judge Manton, rendered May 23, 1919, and apparently not reported).. 10
Northampton Trust Co. *v.* Northampton Traction Co., 112 Atl. (Pa. St.), 871 6
Northwestern Mutual Life Ins. Co. *v.* McCue, 223 U. S., 234 19
Powers *v.* Raymond, 137 Mass., 483 34
Pritchard *v.* Norton, 106 U. S., 124.....49, 50
Pray *v.* Todd, 71 N. Y. App. Div., 391 58
Robinson *v.* W. Va. Loan Co., 90 Fed., 770 .. 40
Roldan *v.* Power, 14 Misc. (N. Y.), 480..... 51
Rolling Mill *v.* Ore & Steel Co., 152 U. S., 596.. 52
Rouse *v.* Letcher, 156 U. S., 47 6
Scott *v.* Neely, 140 U. S., 106.....
.....14, 16, 19, 20, 21, 22, 23, 35
Sill *v.* Kentucky Coal & Timber Development Co., 11 Del. Ch., 93 35
Smith *v.* Railroad Co., 99 U. S., 398 .....11, 12
Smith *v.* Felton, 43 N. Y., 419 53
Steel *v.* Inman, 164 App. Div., N. Y., 146 34
Swan *v.* Mutual Reserve Fund Life Assn., 20 App. Div., 255 (aff'd 155 N. Y., 9)..... 34
Texas Consol. Compress & Mfg. Assn. *v.* Storrow, 92 Fed., 5 13
Thompson *v.* Railroad Cos., 6 Wall., 134 26
Tierney *v.* The Peerless Shoe Co., 33 Misc. (N. Y.), 803 51

PAGE

D. A. Tompkins Co. *v.* Catawba Mills, 82 Fed., 780 ..... 18, 29
Truax *v.* Corrigan, U. S. Supreme Court Advance Opinions, Jan. 16, 1922, 132 32
Van Norden *v.* Morton, 99 U. S., 378 41
Wehrman *v.* Conklin, 155 U. S., 314 41
Whitmer *v.* Whitmer, 11 Delaware Ch. Rpts., 185 30
Woods *v.* Sizer, 102 Misc. (N. Y.), 453 50
Zuber *v.* Micmac Gold Mining Co., 180 Fed., 625 ..... 39, 41

STATUTES.

Bankruptcy Act of 1897 31
Delaware, General Corporation Law of, Sec. 16 56
Delaware, General Corporation Law of, Sec. 18 57
Delaware, Constitution of, Article IV, Sec. 21 .. 29
Delaware, Revised Code of (1915), Sec. 3883 2, 8, 9
Delaware, Revised Code of (1915), Sec. 3884 9
Mississippi, Code of (1880), Sec. 1843 16
Mississippi, Code of (1880), Sec. 1845 16
New York, Civil Practice Act of, Sec. 267 50
New York, General Corporations Law of, Sec. 91 33
United States Constitution, Sec. 8, Subd. 9, Art. I and Sec. 1, Art. III, ... 31
United States Constitution, Seventh Amendment 14, 15, 24
United States Revised Statutes, Sec. 723 19

TEXTS.

22 A. & E. Ency. of Law, 907 58
12 *Corpus Juris*, 786 31
15 *Corpus Juris*, 1373 33
15 *Corpus Juris*, 1389 34
15 *Corpus Juris*, 1390 35
25 *Corpus Juris*, 841 36
High on Receivers, 4th Ed., p. 10, Sec. 6 39

PAGE

Kent's Comm. 58
1 Pomeroy's Equity Jurisprudence (4th Ed.), p. 3602, Sec. 1533 12
1 Pomeroy's Equity Jurisprudence (4th Ed.), p. 3375, Sec. 1423; and p. 3513, Sec. 1492 .. 39
Story's Conflict of Laws, Sec. 332 49
1 Tardy's Smith on Receivers (2nd Ed.) p. 17, Sec. 4; p. 51, Sec. 14 39
Thompson on Corporations 58

Argued by
Lindley M. Garrison.

Supreme Court of the United States

OCTOBER TERM—1922.

THE PUSEY AND JONES COMPANY (a corporation),
Petitioner,

against

HANS KARLUF HANSSEN,
Respondent,

and

JACOB PREBENSEN, JR., H. KJERSCHOW, HARRY BORTHEN, A/S TROMP, A/S MARITIM, A/S HAUG, A/S MERCATOR, A/S SORLANDSKE LLOYD, and E. & N. CHR. EVENSEN,
Intervenors-Respondents.

No. 431.

On writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit.

BRIEF FOR PETITIONER.

Statement of the Case.

The original bill in this cause which is now before this Court on writ of certiorari was brought by respondent Hanssen in the United States Dis-

trict Court for the District of Delaware against petitioner, The Pusey and Jones Company.

Hanssen alleges in his bill that he is a creditor and stockholder of The Pusey and Jones Company, that the bill is prosecuted on behalf of all other stockholders and creditors of The Pusey and Jones Company who may contribute to the expense of and become parties to the suit, that The Pusey and Jones Company is insolvent, that it is not a corporation for public improvement, and that the suit is brought under Section 3883 of the Revised Code of Delaware (1915), which statute is hereinafter set forth in full at page 7, together with the only other related statutory provision. The relief prayed in the bill is (Rec., p. 22):

1. The appointment of a receiver or receivers for the petitioner for the purposes and with the powers enumerated in the statute and such further powers as the Court should deem necessary and proper.

2. A perpetual injunction to restrain petitioner, its directors, officers and agents, from conducting any of the business of the corporation, from receiving and collecting any money due it and from interfering with its business.

3. A decree requiring this petitioner to execute and deliver to complainant a certificate or certificates for 7,200 shares of its preferred stock.

4. Authorization and direction that the receiver or receivers proceed by law to set aside a certain judgment alleged to have been suffered to be entered in favor of the Baltimore Dry Dock & Shipbuilding Company against this petitioner and

to make all proper defense to the action wherein said judgment was obtained.

History of Proceeding.

On the filing of the bill on June 9, 1921, Hanssen moved *ex parte* for the appointment of a receiver or receivers (Rec., p. 78); and the District Court thereupon *ex parte* appointed Willard Saulsbury and Charles B. Evans, of Wilmington, Delaware, receivers of the Pusey & Jones Company, as prayed in the bill, and ordered the Company to show cause on June 18, 1921, why the receivers should not be continued during the pendency of the cause (Rec., pp. 79-82).

Thereupon the Company, on June 11, 1921, moved for an order vacating the receivership upon the grounds that the complainant was not a stockholder or creditor; that the judgment of Baltimore Dry Dock & Shipbuilding Company was not improperly procured; and that the allegations as to petitioner's insolvency were untrue (Rec., p. 83). That motion was denied on June 13, 1921 (Rec., pp. 87-88).

On June 18, 1921, the Company filed its answer to the bill of complaint, among other things alleging its principal place of business to be in the City of New York, denying that complainant was a stockholder or creditor, denying its insolvency, and alleging that it had a surplus, over all its obligations, of several million dollars (Rec., pp. 137-149).

The Company in its said answer also asserted that it was entitled to a trial by jury in an action at law under the Constitution of the United States on the question whether the complainant was a creditor of the company (Rec., p. 147); *that the proceeding might not be maintained in equity in*

the courts of the United States (Rec., p. 147); *and that the District Court had no jurisdiction to entertain the proceeding, it being one neither at law nor in equity* (Rec., p. 148).

On June 18 the order to show cause why the receivers should not be continued in office *pendente lite* was heard, on bill, answer and affidavits (Rec., p. 517); and on August 1, 1921, the District Court made a decree confirming the order of June 9, 1921, appointing the receivers and continuing them *pendente lite* (Rec., p. 603).

Appeal was taken from this decree; and on March 15, 1922, the decree of the District Court was affirmed by the Circuit Court of Appeals for the Third Circuit. The writ of certiorari in this cause was issued to review this determination (Rec., p. 652).

The bill was sustained by both the District Court and the Circuit Court of Appeals as a creditor's bill in equity cognizable by the Federal courts under authority of the Delaware statute. Both courts below have held that the issues as to whether or not Hanssen is a creditor must be determined in equity. The company, therefore, has been deprived of the right seasonably demanded by it, to a common law trial of these issues.

Hanssen's claim to be a creditor was rested on the allegation that he was the transferee of certain notes made by the Pusey & Jones Company. This alleged transfer was from Hannevig, the former president of the Company. At the time of the transfer, these notes had passed maturity, but their collection had been extended by a collateral agreement to a date later than the commencement of this proceeding. The company asserted as offsets exceeding the aggregate of the notes certain claims

against Hannevig existing before the transfer. (See Fifth Point, *post.*) The lower courts declined to find that Hanssen was a stockholder of the Pusey & Jones Company. (See Sixth Point, p. 53, *post.*)

Neither the District Court nor the Circuit Court of Appeals passed upon the question whether Hanssen was a stockholder of the company (Rec., pp. 521, 650).

The Intervenors.

Intervenors-respondents were given leave to intervene as parties complainant by order dated July 6, 1921, after the company's answer was filed (Rec., p. 509). Hanssen alleges that he acted as representative of these intervenors-respondents in bringing his bill and that they are the real parties in interest. This is also their claim (Rec., pp. 501-503); and whatever is said in this brief regarding Hanssen applies to them equally. They have served no bill of complaint.

The United States Shipping Board Emergency Fleet Corporation was given leave to intervene as a party complainant, by the District Court by order, dated October 8, 1921, some two months after the entry of the decree of the District Court (Rec., p. 635). It has not served any bill of complaint, and questions as to its rights were not passed upon by either court below. It is not named a respondent for this reason, although its solicitors have been duly served with this brief and with all papers in connection with the writ of certiorari.

While we do not see how it is possible to argue that if the case at bar fails because of lack of jurisdiction in the court at the time of its inception, it may be saved because of the subsequent intervention of the United States Shipping Board

Emergency Fleet Corporation, we point out that any such argument would be unsound. An intervening proceeding is always ancillary and supplemental under jurisdiction already subsisting. (*Rouse* v. *Letcher*, 156 U. S., 47; *Adler* v. *Seaman*, 266 Fed., 828, 832.) An intervenor is bound to take the suit as he finds it. *Northampton Trust Co.* v. *Northampton Traction Co.*, 112 Atl. (Pa. St.), 871. Hence, the filing of an intervening petition, even if in time, cannot save the original bill if that is bad or without jurisdiction. (*Atlanta etc., Co.* v. *Carolina Cement Co.*, 140 Ga., 650.) An intervenor is let in solely for the purpose of having his right to the property or fund adjudicated under the jurisdiction acquired between the original parties. (*Mesa Mellon Growers Asso.* v. *Byrnes*, 211 Ill. Apps., 236; *Boston & M. R. R.* v. *Sullivan*, 275 Fed., 890). Moreover, the Shipping Board has asked for no relief, has sought no foreclosure, has tendered no issue, and has not offered to put itself on any parity with general creditors.

Principal Questions Presented.

The Pusey & Jones Company claims as the fundamental errors in the decision below, the following:

(1) The Delaware statute did not confer on the Federal court the jurisdiction which it undertook to exercise, to wit: Jurisdiction at the instance of an alleged simple contract creditor, who had no specific lien or security and whose claim was disputed, to maintain this action and secure the appointment of receivers therein.

(2) The action of the courts below improperly deprived the Pusey & Jones Company of its con-

stitutional right to trial by jury of the common law issue as to whether or not Hanssen was a contract creditor of the company.

(3) The action of the courts below improperly permitted the state statute to obliterate the line of demarcation, in substance and procedure, which exists in a Federal court between causes of action at law and causes of action in equity; improperly mingled a cause of action at law with an alleged cause of action in equity; and improperly committed its decision to the equity side. Moreover, the power conferred by that statute are visitorial, rather than judicial.

(4) Since the bill of complaint prayed for no final and ultimate relief, it was not cognizable by a Federal court in equity, and the state statute could not confer jurisdiction on a Federal court in equity to entertain such a bill.

(5) The application, made below, of the Delaware statute to the Federal court, is unconstitutional.

(6) The claim of Hanssen to have the status of a creditor, within the meaning of the Delaware statute, is irrelevant, was denied in its entirety, and was not substantiated.

(7) The claim of Hanssen to have the status of a stockholder, within the meaning of the Delaware statute, is without merit, and raises no question for review at this time, since that claim did not enter into the discretion exercised by the District Court.

Specifications of Error.

These are the substantial questions presented by the assignments of error which appear at pages

605 to 616 of the Record. For brevity's sake we will not set out these assignments of error here, although we rest his appeal on each of them, but we respectfully refer the Court particularly to those assignments numbered 1, 10, 11, 19, 20, 29, 37 and 38.

FIRST POINT.

Hanssen's claim is at best but that of an alleged simple contract creditor of the Pusey & Jones Company. His claim is disputed in its entirety and has not been reduced to judgment. He holds no lien upon the property of the company. The company made timely demand of a common law trial by jury of Hanssen's claim.

Hence, the United States District Court sitting in equity should not have entertained his bill, and had no jurisdiction to do so under the Statute of Delaware or otherwise.

The Delaware statute under which the action is sought to be maintained reads as follows:

> "Whenever a corporation shall be insolvent, the Chancellor, on the aplication and for the benefit of any creditor or stockholder thereof, may, at any time, in his discretion, appoint one or more persons to be receivers of and for such corporation, to take charge of the estate, effects, business and affairs thereof, and to collect the outstanding debts, claims, and property due and belonging to the company with power to prosecute and defend, in the name of the corporation or otherwise, all claims or suits, to appoint an agent or agents under them, and to do all other acts which might be done by such corporation and may be necessary and proper; the powers of such

receivers to be such and continued so long as the Chancellor shall think necessary; provided, however, that the provisions of this Section shall not apply to corporations for public improvement." (Rev. Code Del., 1915, Sec. 3883.)

The next and only related section of the Code provides as follows:

"The receiver or receivers appointed by the Chancellor, of and for any corporation created by or existing under the laws of the State of Delaware, and the successor or successors of any such receiver or receivers, shall upon his or their appointment and qualifications, and the survivors or survivor of such receivers shall upon the death, resignation or discharge of any co-receiver or co-recivers, be vested by operation of law, without any act or deed, with the title of such corporation to all its books, papers and documents, interests in patents, patent rights, copyrights and trademarks, rights of action arising upon contracts or from the unlawful taking or detention of or injury to property of such corporation, and other property, real, personal or mixed of whatsoever nature, kind, class or description, and wheresoever situate, except real estate situate outside the State.

"The receiver or receivers appointed by the Chancellor as aforesaid shall, within twenty days from the date of his or their qualification, file in the office of the Recorder in each County in this State, in which any real estate belonging to such corporation may be situated, a certified copy of his or their appointment and qualification.

"The provisions of this section shall not apply to receivers appointed *pendente lite*." (Rev. Code Del. [1915], Sec. 3884.)

Hence, we have here a case where a Federal

court—on the complaint of one who applies as a simple creditor and where the defendant denies that he is a creditor at all—has appointed receivers for a corporation on affidavits, without a trial of the validity of the claim or of the charge of insolvency, and without the defendant being permitted to produce oral testimony or to cross examine the parties making the charges of insolvency on behalf of the alleged creditor. Relief awardable in equity only after execution return unsatisfied, has preceded trial.

In this summary and drastic method the officers and directors of the company have been divested of the control entrusted to them by the stockholders.

Our first proposition is that the Delaware statute cannot be used in a Federal court to authorize any such result in a case like the present. Its inapplicability, in law and justice, is emphasized by the fact that Hanssen's custody of the notes was solely for purposes of collateral security and that Hannevig who turned over the notes to him after their maturity was then, and still is, indebted to the company in an amount largely exceeding the amount of the notes (Rec., pp. 485, 489, 495, 375, 412).

Our proposition, we submit, has been upheld by this Court, by the Federal courts of inferior jurisdiction, by the courts of almost every State in the Union and by the authoritative text writers. It expresses immemorial limitations on the jurisdiction of courts of equity. It recognizes the ancient right to the trial of common law demands by common law courts and a common law jury. It preserves the right of the defendant to pay the claim if, after common law trial, it be held valid.

It protects the right of the owner of property to retain possession except under due process of law.

"Nothing is better settled," said this Court, in *Smith* v. *Railroad Co.*, 99 U. S., 398, 401, than that a creditor's bill

> "must be preceded by a judgment at law establishing the measure and validity of the demand of the complainant for which he seeks satisfaction in chancery."

The first four sentences of the decision of this Court in *Hollins* v. *Brierfield Coal and Iron Co.*, 150 U. S., 371, dispose adversely of practically every contention which Hanssen can make either under general principles of equity or under the Delaware statute. Mr. Justice Brewer opened the decision of this Court as follows (p. 378):

> "The plaintiffs were simple contract creditors of the company; their claims had not been reduced to judgment, and they had no express lien by mortgage, trust deed, or otherwise. It is the settled law of this court that such creditors cannot come into a court of equity to obtain the seizure of the property of their debtor, and its application to the satisfaction of their claims; *and this, notwithstanding a statute of the State may authorize such a proceeding in the courts of the State. The line of demarcation between equitable and legal remedies in the Federal courts cannot be obliterated by state legislation.* *Scott* v. *Neely*, 140 U. S., 106; *Cates* v. *Allen*, 149 U. S., 451. Nor is it otherwise in case the debtor is a corporation, and an unpaid stock subscription is sought to be reached. *National Tube Works Company* v. *Ballou*, 146 U. S., 517; *Swan Land & Cattle Company* v. *Frank*, 148 U. S., 603, 612."

Answering the contention that the funds of the corporation were a trust fund for the benefit of creditors, this Court pointed out that such language was used by way of analogy or metaphor and not to convey the idea that there was a direct or express trust attached to the property, adding (p. 385):

> "Neither the insolvency of the corporation, nor the execution of an illegal trust deed, nor the failure to collect in full all stock subscriptions, nor, all together, gave to these simple contract creditors any lien upon the property of the corporation, nor charged any direct trust thereon."

I.

The Rule in Courts of Equity in the absence of state statutes.

The general rule is thus stated in 4 *Pomeroy's Equity Jurisprudence* (4th Ed.), page 3602, Section 1533:

> "It is the almost universal rule that a creditor's bill, whether to set aside a fraudulent transfer or to reach equitable assets, will not lie in behalf of mere general creditors who have not prosecuted their claims to judgment, nor in any other manner acquired a lien upon the debtor's property."

That this rule is approved and applied by this Court, is clear from the quotations set forth above from the *Smith* and the *Hoilins* cases *supra*. In *Continental Trust Co.* v. *Toledo etc. R. Co.*, 82 Fed., 642 (aff'd 95 Fed., 497), the present Chief Justice of this Court referred to this rule as "so clearly settled in the federal equitable jurisprudence" as to be "conclusive" (p. 661).

In addition, there is a long and unbroken line of

decisions in the Federal courts of inferior jurisdiction to the same effect. Among them are:

Maxwell v. *McDaniels*, 184 Fed., 311;
American Can Co. v. *Erie Preserving Co.*, 171 Fed., 540;
Nesbit v. *North Georgia Electric Co.*, 156 Fed., 979;
Texas Consol. Compress & Manufacturing Assn. v. *Storrow*, 92 Fed., 5.

The allegation that the alleged debtor has conveyed property in fraud of creditors is no more effective than the allegation of insolvency to give a Federal court in equity jurisdiction to seize the property of the alleged debtor at the instance of a simple contract creditor. As said in *Maxwell v. McDaniel*, 184 Fed., 311 (p. 314):

> "At the time the receivers were appointed the complainant's claim had not been reduced to judgment. A Federal Court of equity was therefore without jurisdiction to hear his complaint that his debtor had made a fraudulent conveyance of his property. *Scott* v. *Neely*, 140 U. S., 108; *Cates* v. *Allen*, 149 U. S., 451."

In *Gillespie* v. *Riggs*, 253 Fed., C. C. A., 943, it was held that such an application by a simple contract creditor on the ground of an attempt to defraud creditors "comes under no recognized head of equity jurisprudence" (p. 945).

II.

The Rule in the Federal Courts under state enabling statutes.

Three fundamental principles have always been steadily maintained by this Court as essential to

the independence and constitutional limitations of the Federal courts. In the present instance, all three have, we respectfully submit, been gravely challenged by the decision below. These principles are:

(1) "It is well settled that the jurisdiction of the Federal courts, sitting as courts of equity, is neither enlarged nor diminished by state legislation" (*Mississippi Mills* v. *Cohn*, 150 U. S., 202, 204).

(2) "The line of demarcation between equitable and legal remedies in the Federal courts cannot be obliterated by state legislation" (*Hollins* v. *Brierfield Coal & Iron Co.*, 150 U. S., 371, 378).

(3) The United States Constitution, in its Seventh Amendment, puts the binding restriction upon the Federal courts that "in suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved." This Amendment, though not binding state courts, concludes the Federal courts; and the Federal courts cannot deal with rights or remedies save in accordance therewith. As said in *Scott* v. *Neely*, 140 U. S., 106, 109:

> "In the Federal courts this right cannot be dispensed with, except by the assent of the parties entitled to it, nor can it be impaired by any blending with a claim, properly cognizable at law, of a demand for equitable relief in aid of the legal action or during its pendency."

In the present case, Hanssen claims to be a creditor of the Pusey & Jones Company upon certain promissory notes. The Pusey & Jones Company

denies the claim. From time immemorial, that issue typifies the action at law and the right of trial by jury. From time immemorial, also, a court of equity has not undertaken (in the absence of legislation) to deny the right to a jury trial in such case, and has not been persuaded to do so merely because the defendant is said to be insolvent or acting in fraud of creditors. This immemorial law has been embodied in the United States Constitution and no state statute can now give a Federal court of equity extra-constitutional powers.

The test to be used in the application of these principles under the Seventh Amendment is the common law as it existed when the Constitution was adopted. As said in *Mississippi Mills* v. *Cohn*, 150 U. S., 202, 205:

> "The equity jurisdiction conferred on the Federal courts is the same that the High Court of Chancery in England possesses; is subject to neither limitation or restraint by state legislation, and is uniform throughout the different states of the Union."

In conformity with the three principles above outlined it has been repeatedly held by this Court that a Federal court cannot derive any equitable power from a state statute authorizing a simple contract creditor whose claim is disputed and who has no lien to enforce his claim by proceedings in equity.

In *Hollins* v. *Brierfield Coal & Iron Co.*, 150 U. S., 371 (*supra*), to be sure, no state statute was directly involved; but this Court was merely stating the rule, which it had recently settled in two other cases so closely analogous to ours as to be indistinguishable in principle:

Scott v. *Neely*, 140 U. S., 106;
Cates v. *Allen*, 149 U. E., 451.

Scott v. *Neely* was an action by simple contract creditors who had not reduced their disputed claim to judgment and who had no lien upon the property of the alleged debtor, to subject the property of defendants to the payment of the alleged debt in advance of any proceedings at law. The complainants relied upon Sections 1843 and 1845 of the Code of Mississippi of 1880, which authorized a simple contract creditor to present a creditor's bill to set aside any fraudulent conveyances and devices, and gave such creditor a lien upon the property of the debtor from the time of filing the bill.

By a unanimous Court, Mr. Justice Field writing the opinion, it was held that despite these statutory provisions the Federal courts had no jurisdiction of the suit; and this Court said (p. 113):

> "In all cases where a court of equity interferes to aid the enforcement of a remedy at law, there must be an acknowledged debt, or one established by a judgment rendered, accompanied by a right to the appropriation of the property of the debtor for its payment, or, to speak with greater accuracy, there must be, in addition to such acknowledged or established debt, an interest in the property or a lien thereon created by contract or by some distinct legal proceeding."

Cates v. *Allen*, 149 U. S., 451, *supra*, was a suit under the same statutory provisions of the Mississippi Code. It was originally brought in the State court and was thereafter removed to the Federal court, on the ground of diversity of citi-

zenship. The complainants were simple contract creditors, who had not reduced their claim to judgment but sought to set aside certain fraudulent conveyances. This Court held that the bill could not be maintained in the Federal court; and said (p. 457):

> "The existence of judgment, or of judgment and execution, is necessary, first, as adjudicating and definitely establishing the legal demand, and, second, as exhausting the legal remedy."

And again (p. 458):

> "The fact that section 1845 aims to create a lien by the filing of the bill does not affect the question, for in order to invoke equity interposition in the United States courts the lien must exist at the time the bill is filed and form its basis, and to allow a lien resulting from the issue of process to constitute such ground would be to permit state legislation to withdraw all actions at law from the one court to the other, and unite legal and equitable claims in the same action, which cannot be allowed in the practice of the courts of the United States, in which *the distinction between law and equity is a matter of substance, and not merely of form and procedure.*"

In conformity with these decisions, the same rule has been applied in a number of cases by various Circuit Courts of Appeals and by other Federal courts, where state statutes of a similar nature have been involved.

Davidson-Wesson Implement Co., Ltd. v. *Parlin & Orendorff Co.* (C. C. A., 5th

Circuit, 1905), 141 Fed., 37;

Jacobs et al. v. *Mexican Sugar Co.* (C. C., New Jersey, 1904), 130 Fed., 589;

Harrison et al. v. *Farmers' Loan and Trust Company of New York* (C. C. A., 5th Circuit, 1899), 94 Fed., 728;

D. A. Tompkins Co. v. *Catawba Mills* (C. C., So. Car., 1897), 82 Fed., 780;

Morrow Shoe Mfg. Co. v. *New England Shoe Co.* (C. C. A., 7th Circuit, 1893), 57 Fed., 685; affirmed on rehearing, 60 Fed., 341;

Atlanta & F. R. Co. v. *Western Ry. Co.* (C. C. A., 5th Circuit, 1892), 50 Fed., 790;

Matthews Slate Co. v. *Matthews*, 148 Fed. (D. C., Mass.), 490;

III.

Decisions claimed to be contrary, distinguished.

(1) *Darragh* v. *H. Wetter Mfg. Co.* (C. C. A., 8th Cir., 1897), 78 Fed., 7, is easily distinguishable upon the grounds:

(a) The corporation expressly consented to the appointment of a receiver for purpose of liquidation, and did not deny the claim of the H. Wetter Manufacturing Company as a creditor. Hence there was no common law issue as to the corporation's liability to the H. Wetter Manufacturing Company.

(b) The Arkansas statute there involved was very exceptional; and rendered void any common law judgment against the corporation if attacked within ninety days. This practically repealed the remedy at law and deprived a common law judgment of its conclusive, evidentiary character.

(c) The attempt to nullify the appointment

> of receivers for the corporation was made by a stockholder thereof in a collateral proceeding. It was held that he had no cause of complaint.

Moreover, the reasoning in that case proceeds upon a clear misconstruction of *Cowley* v. *Railroad Co.*, *Scott* v. *Neely* and *Cates* v. *Allen*. Those cases, Mr. Justice Sanborn says, were decided upon the basis of Section 723 of the Revised Statutes, which provides that

> "suits in equity shall not be sustained in either of the courts of the United States in any case where a plain, adequate, and complete remedy may be had at law."

In *Scott* v. *Neely*, however, the complainant united with his demand for the payment of the alleged debt, "a proceeding to set aside alleged fraudulent conveyances of the defendants." We are unable to perceive how the complainant could have hoped for *any* relief *at law* upon this branch of the case, let alone "plain, adequate and complete" relief. And in *Cates* v. *Allen*, the bill prayed that an alleged fraudulent assignment of property should be set aside; "for an injunction; for a writ of sequestration; for a receiver; that the filing of the bill be held to give complainants the first lien on the effects of the said debtors in the hands of the assignees, or either of the parties or any other person; and for general relief." Again we are unable to perceive how the decision could possibly have gone against the complainants upon the theory that they had an adequate remedy at law.

Certainly neither one of those decisions by this Court was put upon the ground that the plaintiff

had an adequate remedy at law. The very first paragraph following the statement of facts and the question at issue, in the opinion of Mr. Justice Field in *Scott* v. *Neely*, shows that *the bases of the decision were the constitutional guaranty that a litigant cannot be deprived of his right to a common law trial of common law issues, and the distinction in the Federal courts between law and equity.*

The mistaken construction attempted to be put by *Darragh* v. *H. Wetter Manufacturing Co.* upon *Scott* v. *Neely* and *Cates* v. *Allen*, was considered at length and rejected in the later case of *Jacobs* v. *Mexican Sugar Co.* (C. C. New Jersey, 1904), 130 Fed., 589.

(2) The case of *Jones* v. *Mutual Fidelity Co.* (C. C. Del., 1903), 123 Fed., 506, much relied on by opposing counsel, may be readily distinguished on a number of grounds:

(a) The case came up on demurrer, which necessarily admitted all the allegations of the complaint. Hence, as presented, there was no common law issue as to the defendant's liability to the plaintiff.

(b) The *primary right* asserted by the complainants in that case was *equitable*, not legal. The bill of complaint charged that the complainants had been induced *by the fraud of the defendant corporation* to purchase certain of its certificates of investments and obligations. The complainants, therefore, had an elementary right in equity to be relieved (and they prayed to be relieved) as to this purchase and to "have a lien upon the assets of the said Mutual Fidelity Company for the amounts that they have paid into the said company, and for an accounting and injunction." The case, therefore, is an instance where the complainants had an equitable lien

upon the property of the defendant and were suing for an equitable rescission—which has always been a primary head of equitable jurisdiction.

(c) Finally, the constitutional question was not raised. The hearing was on demurrer, and no denial by the defendant raised any issue of fact to be settled by a jury. A question of such a character is waived if not properly presented. (*Metropolitan Ry. Receivership*, 208 U. S., 90, 109.)

Moreover, the reasoning of the opinion in the *Jones* case is, we submit, unsound, or, at least, inapplicable as regards the present case.

To apply that reasoning to the facts of the present case seems to us merely to play upon the words "rights" and "remedies." Any so-called "equitable right" in the present case is really nothing but an attempted "equitable remedy." It is not substantive but adjectival. It partakes not of the cause of action but of the relief. Hanssen's only cause of action is to recover his alleged debt. Pending proof of the debt, he asks a receivership. On its very face that request is, like an attachment, purely incidental to collection of any judgment Hanssen may recover. It is not the assertion of a substantive right. It is merely remedial. The appointment of the receiver neither satisfies nor discharges the debt. It does not even adjudicate finally its existence.

The reasoning and consequences of the *Jones* and *Darragh* cases as applied to a purely legal pecuniary demand were rejected with striking prevision by Mr. Justice Field in *Scott* v. *Neely*, *supra* (140 U. S., 106, 114):

"Upon the contention of the complainants

> it is not perceived why all actions at law, even for injuries to persons or property, may not be withdrawn by the State from a court of law to a court of equity, by allowing a lien upon the property of the defendants on the issue of process at the commencement of the action, and authorizing the court to direct a sale of the whole or a portion thereof, in its discretion, to pay the damages recovered, and to set aside any obstacles to their satisfaction from fraudulent conveyances of the wrongdoer. Whatever control the State may exercise over proceedings in its own courts, such a union of legal and equitable relief in the same action is not allowed in the practise of the Federal courts."

(3) *McGraw* v. *Mott* (C. C. A., 4th Circuit, 1910), 179 Fed., 646 falls within two well recognized exceptions: (1) Where the defendant has submitted to the jurisdiction of the court, the decree is not open to collateral attack by third parties. (2) Under such a statute as we are considering, a corporate defendant may waive objection to the jurisdiction either in terms or by conduct.

(1) Some of the judges in the cases just cited have suggested that the decisions in the *Scott, Cates* and *Hollins* cases, *supra*, are in part or wholly overruled by *Cowley* v. *Northern Pacific Railroad Co.*, 159 U. S., 569, where it was said that "a party by going into a national court does not lose any right or appropriate remedy of which he might have availed himself in the State courts of the same locality" (p. 583). That case was not a creditor's bill at all, but was merely an action to impeach a state court judgment for fraud. This Court held that, if the proper diversity of citizenship were shown, the suit to impeach could be

maintained in the Federal court quite as properly as in the state court.

Adequate reply to any suggestion that this *Cowley* case overrules the *Cates* and *Hollins* cases has been made by Circuit Judge Lowell in *Mathews Slate Co.* v. *Mathews*, 148 Fed., 490 (p. 491):

> "Following certain expressions of the Circuit Court of Appeals for the Eighth Circuit in *Darragh* v. *Wetter Mfg. Co.*, the defendant urges that *Cates* v. *Allen* has been questioned and, in effect, overruled. I can find no trace of this. *The case has often been cited by the Supreme Court, always with approval, never with doubt.* The authority of *Darragh* v. *Wetter Mfg. Co.*, and the cases which have followed it in the same court, is thus considerably weakened, indeed, as being based upon a misconception of *Cates* v. *Allen*."

The theory that a party has nothing to lose by his choice of tribunals is a merely general expression, to which, as every judge and lawyer knows, there are many exceptions. Indeed, this case comes squarely within the restrictions on this very principle as declared by this Court in *Louisville & N. R. R. Co.* v. *Western Union Tel. Co.*, 234 U. S., 369, 376.

The judges in many inferior courts have not interpreted the *Cowley* case, as overruling the *Scott*, *Cates* and *Hollins* cases. See the opinions in *Gillespie* v. *Riggs* (C. C. A., 4th Cir., 1918), 253 Fed., 943; *Davis* v. *Hayden* (C. C. A., 4th Cir.), 238 Fed., 731; *Mathews Slate Co.* v. *Mathews*, 148 Fed., 490; *Continental Trust Co.* v. *Toledo, St. L. & K. C. R. Co.*, 82 Fed., 642, 661 (opinion by Mr. Chief Justice Taft, then a Circuit Judge), and a score of other cases.

SECOND POINT.

The orders below rest on an interpretation of the Delaware Statute, which purports to enlarge the jurisdiction of the Federal Court in equity and to empower it to determine an ordinary common law claim under the guise of merely supplying an auxiliary remedy in equity. That interpretation obliterates the line of demarcation in the Federal courts between common law and equitable causes and deprives the defendant of its constitutional right to a jury trial under the Seventh Amendment to the United States Constitution.

In *Grand Chute* v. *Winegar*, 15 Wall., 373, Mr. Justice Hunt, in delivering the opinion of the Court, said (p. 375):

> "The right to a trial by jury is a great constitutional right, and it is only in exceptional cases and for specified causes that a party may be deprived of it."

The application of the Delaware statute, if applicable at all, must be on one of three possible theories, viz.: (1) That it merely adds an equitable remedy in aid of a common law cause of action; (2) that it enlarges the jurisdiction of the Federal court in equity; or (3) that it confers visitorial power over corporations upon "the Chancellor."

We submit that, on none of these theories, can the statute be utilized as it has been utilized in the courts below.

I.

If the statute be interpreted as merely providing an equitable remedy in aid of a legal cause of action, the application made of it below is clearly improper in a Federal court, since it deprived the defendant of its constitutional right to trial by a jury and obliterated the distinction in Federal courts between common law and equitable causes of action.

Hanssen has, at most, merely a disputed pecuniary demand upon certain promissory notes. The right and the issue thereon are typical of the common law case, triable from time immemorial by a jury. Hanssen had no equitable cause of action as such. His right, if any, was a right to payment of the notes. That was the foundation of his case. He could have maintained no suit in equity to enforce the payment of the notes. If, therefore, the statute be interpreted as adding an equitable remedy to the legal remedy and as allowing the equitable remedy to be pursued to the exclusion of the legal remedy without any prior trial of the legal cause of action and the issues therein involved, obviously the defendant is cut off in the Federal court from its constitutional right of trial by jury, and a way has been found to convert all legal causes of action into equitable causes of action merely by providing a new and additional equitable remedy.

Nor can the result be changed by calling the new remedy a new right. The fact remains that, whatever name is used, the proceeding is essentially ancillary and remedial,—adjectival rather than substantive.

II.

In the courts below, however, the application of the Delaware statute has rather been rested on an interpretation of it as enlarging the jurisdiction of the court of equity.

No one disputes that as a general proposition a State may create new rights and prescribe the remedies in enforcing them; and that, if those rights are of an equitable character and within the general class of rights administered in equity, the Federal courts may enforce them in equity.

But this does not mean that any State can, in addition to creating a new right, enlarge the jurisdiction of a Federal court of equity, or by giving a so-called new right to a plaintiff, deprive a defendant of his rights in a Federal court as preserved by the Constitution of the United States. Much less does it mean that a State can by fiat convert a legal cause of action into an equitable cause of action and thereby abolish the statutory distinctions in Federal courts with respect to substance and procedure between common law and equitable causes.

In *Thompson* v. *Railroad Cos.*, 6 Wall., 134, it was said, in reversing a decree in equity for want of jurisdiction (p. 137):

> "Thus, an action at law, which sought solely to recover damages for a breach of contract, was transmuted into a suit in equity, and the defendant deprived of the constitutional privilege of trial by jury."

Furthermore, the peculiar features of this Delaware statute stamp it as a most remarkable enlargement of jurisdiction.

The statute reads as if it were a mere introduc-

tion to further provisions looking to a liquidation; but the statute proceeds no further than this introduction. It provides for neither suit, notice, process, trial nor judgment. It authorizes the Chancellor, not by suit but upon mere personal application to him, to appoint receivers to take "charge of the estate, effects, business and affairs" of the corporation, to collect its debts, to prosecute and defend actions, to appoint managing agents, "and to do all other acts which might be done by such corporation, and may be necessary and proper." Such receivership is to be continued "so long as the Chancellor shall think necessary." To what end the receivership shall be conducted, or what shall be ultimately done with the corporation and its affairs, is not stated. Apparently the mere appointment of receivers and the subsequent unlimited management of the corporation by the receivers in substitution for the board of directors is the end contemplated. Executive rather than judicial power is involved. (See Subdivision III, p. 28 *post*.) Receivers may be appointed "*pendente lite*," but there is no *lis pendens*. The outcome is merely whatever "the Chancellor shall think necessary." The conception of a cause of action as a means of securing an adjudication of rights alleged to have been invaded, is not followed.

Such a statute, if the proceeding be deemed judicial and not administrative, is necessarily an enlargement of jurisdiction—an enlargement for which no parallel in legislation can be found.

Judge Morris has himself admitted in *Adler* v. *Campeche Laguna Corporation*, 257 Fed., 789, 791, that "the Delaware statute *enlarges the jurisdiction* of the Court of Chancery."

As illustrating the settled judicial opinion that state statutes of a similar character are *enlargements of equitable jurisdiction rather than of recognized equitable rights and hence are not applicable in the Federal courts*, we may cite the interpretation given by Circuit Judge Lowell in *Mathews Slate Co.* v. *Mathews*, 148 Fed., 190, to a Massachusetts statute authorizing the state courts to entertain in equity

> "suits by creditors to reach and apply, in payment of a debt, any property, right, title or interest, legal or equitable, of a debtor, within or without this commonwealth, which cannot be reached to be attached or taken on execution in an action at law."

Obviously this statute did not go as far as the Delaware statute because it did not provide for the unlimited substitution of a chancellor for the board of directors; and because the state courts had interpreted the statute as leaving the defendant his right of jury trial notwithstanding that it contemplated a proceeding in equity. Nevertheless, Judge Lowell held that the statute was inapplicable in a Federal court to the case of a common-law creditor whose claim was disputed and not reduced to judgment, and in a remarkably well-reasoned opinion said (p. 195):

> "But the decision of the Supreme Court in *Cates* v. *Allen*, and in other cases above referred to, was not rested wholly upon the unconstitutionality of the statutory proceeding. Moreover, to permit the complainant to proceed here in equity, while the defendant retains a right to jury trial, not merely for the trial of issues framed by the court, but in general as guaranteed by the Constitution,

would so disarrange federal procedure in equity as to leave it at the mercy of any state statute which does not contravene the seventh amendment."

Other decisions holding that state statutes of this character are enlargements of equitable jurisdiction rather than of recognized equitable rights and hence are inapplicable in Federal courts, may readily be multiplied:

Morrow Shoe Mfg. Co. v. *New England Shoe Co.*, 60 Fed. (C. C. A.), 341, 342;

D. A. Tompkins Co. v. *Catawba Mills*, 82 Fed., 780, 783;

Atlanta & F. R. Co. v. *Western Ry. Co.*, 50 Fed., C. C. A., 790, 795.

III.

A third possible interpretation of the Delaware statute is: That what it provides is visitorial or supervisory power by the State over corporations through the Chancellor of the State.

For generations visitorial powers have been exercised in English law by the Chancellor under the common law, and the Chancellor was the natural repository of visitorial powers. Under the Constitution of Delaware the Chancellor is a high officer of State, in whom by express provision of the Constitution may be vested "all the powers which any law of this State vests in the Chancellor, besides the general powers of the court of chancery." (Article IV, Sec. 21.)

The Delaware statute now relied upon by Hanssen does not confer the power to appoint a receiver on the court of chancery, but on the Chancellor. It

does not provide for a bill in equity in the court of chancery, but for an application to the Chancellor. If an application were made to him by a stockholder or creditor of the corporation, not by bill in equity, nor even by a formal petition entitled in the court of chancery, he would, nevertheless, by the very terms of the statute, be called upon to entertain and dispose of the application. It makes no provision for process, notice, trial or judgment. It presents the whole matter as one personal to the Chancellor. It mentions no court. It does not even provide that the corporation be heard. No requirement for liquidation and no method of liquidation are stated. No final judgment is required.

Moreover, the statute contains no provision for review of any action by the Chancellor, and it contemplates placing him in the position of sole manager and director of the corporation for such period of time as in his uncontrolled discretion he may think proper.

The very fact that, under this statute, the application may be made solely by a stockholder, shows that the statute contemplates a visitorial rather than a judicial power, for a stockholder of an insolvent corporation can gain nothing by its liquidation.

Hence, we submit, an application under this statute is one to the visitorial power, and the relief contemplated is visitorial and executive.

It is true that there are some dicta by the Chancellor in the case of *Whitmer* v. *Whitmer*, 11 Delaware Chancery Reports, 185, to the effect that the proceeding is one in equity; but the point whether the Chancellor was exercising visitorial power or judicial power was not before him, and could not

have been raised in the case, so that his statement was pure dictum. In fact, the only way this question could be raised before the Chancellor of Delaware would be by a discussion of the question whether a particular application, not made in the form of a bill in equity or of a petition in equity, could be entertained by him. We do not understand that there has ever been a decision that it could not.

On the other hand, there have been very numerous decisions during the past twenty years which sustain the theory that this is an exercise of visitorial power. It is familiar law that the insolvency statutes of the various States were superseded by the passage of the Bankruptcy Act of 1897, and that insolvency proceedings could no longer be maintained under State insolvency acts after the adoption of the Bankruptcy Act (*Closser* v. *Strawn*, 227 Fed., 139).

Nevertheless, the Delaware Chancellor has gone on year after year ever since the passage of the Bankruptcy Act, appointing receivers of Delaware corporations under this section of the Delaware statutes. Every such decision, therefore, is sustainable only as an exercise of visitorial power.

Such powers are not exercisable by the United States District Courts, which cannot be vested with the executive or administrative powers of state officers, but only with judicial powers. (See U. S. Constitution, Sec. 8, Subd. 9 of Art. I, and Sec. 1 of Art. III.)

The mere fact that in all reported instances the Delaware courts have, under this statute, proceeded by way of a bill in equity, is no argument in favor of the constitutionality of the act as applied to the Federal court. As said in 12 *Corpus Juris*, 786:

> "Whether or not a particular statute is constitutional is a matter of law, and must be tested, not by what has been done under it, but by what the law authorizes to be done under its provisions."

The right of The Pusey & Jones Company to its business and the free conduct thereof is a property right. (*Truax* v. *Corrigan*, U. S. Supreme Court Advance Opinions, Jan. 16, 1922, 132, 136; *Duplex Printing Press Co.* v. *Deering*, 254 U. S., 443, 465.) Consequently, no State can by statute withdraw the protection of due process of law from such property—much less authorize its seizure by a State or Federal court without due process of law, notice, hearing and judgment. (*Hovey* v. *Elliott*, 167 U. S., 409; *Truax* v. *Corrigan*, U. S. Supreme Court Advance Opinions, Jan. 16, 1922, 132, 137.)

Unless sustainable as an exercise of the power of visitation reserved by the State, this Delaware statute is clearly unconstitutional. But, if sustained on that theory, the power is one that no Federal court can exercise in place of the officer of the State to whom such visitorial powers are entrusted. Under the distribution of governmental powers and functions made by the United States Constitution, a Federal court cannot be burdened with such executive and administrative powers.

THIRD POINT.

The Delaware Statute has never been construed, except in the decisions below, as authorizing a simple contract claimant whose claim is disputed by answer demanding a jury trial and who has no legal or equitable lien on the property of the corporation, to institute a creditor's bill under the statute.

Legislation, which in general terms authorizes a creditor of a corporation to institute a creditor's bill and which does not expressly indicate an intention to include simple contract creditors, is invariably, so far as we can ascertain, construed to refer only to judgment and lien creditors.

In 15 *Corpus Juris*, p. 1373, with reference to the use of the word "creditor" in general statutes authorizing a creditor's bills to set aside a fraudulent conveyance or to enforce claims against equitable assets, etc., the rule is thus stated:

> "Thus the term ('creditor') has been held frequently not to include creditors at large, but to be confined to judgment creditors and those who have in some manner effected a lien on the debtor's property. It is in this sense that the word is used in certain statutes governing procedure and relief."

An illustration may be found in Section 91 of the General Corporations Law of the State of New York which expressly authorizes such an action to be brought "by a creditor of the corporation." The courts of New York have invariably construed the word "creditor" as here used to mean "judgment creditor."

Steel v. *Isman*, 164 App. Div., N. Y., 146;
Moe v. *Thomas McNally Co.*, 138 App. Div., N. Y., 480;
Swan v. *Mutual Reserve Fund Life Assn.*, 20 App. Div., 255 (aff'd 155 N. Y., 9).

Corpus Juris, Vol. 15, page 1389, lists as the "few states" which have by statute authorized the filing of creditor's bills without first recovering a judgment: Connecticut, Louisiana and Massachusetts. Even in Massachusetts it is held that the statute, though providing for proceedings in equity, must be construed so as to leave to the defendant his right of jury trial.

Powers v. *Raymond*, 137 Mass., 483;
Mathews Slate Co. v. *Mathews*, 148 Fed., 490, 494.

As we have already pointed out, right to a jury trial or to have a cause tried in a particular forum may be waived (*Metropolitan Railway Receivership*, 208 U. S., 90, 109).

In the light of these principles we have examined the Delaware decisions and are unable to find any which parallel the construction of the statute adopted in the courts below. In all of them one or more of the vitally distinguishing circumstances appear: either the point was not raised; or the claim of the plaintiff stood admitted on the record in whole or in part; or the claimant had a specific legal or equitable lien on the property of the corporation; or the primary right which he was seeking to enforce was equitable. We find no decision in Delaware holding that a simple contract claimant can, in the absence of these circumstances, maintain an action under the Delaware statute in question; and we find no Delaware decision over-

ruling the right of a defendant who makes timely demand therefor to have the common law issues as to the contract liability tried in a common law action before a common law jury.

Merely piling up Delaware decisions in which the Delaware statute has been the successful basis of a creditor's bill means nothing. The facts and circumstances of each case must be examined; and it must always be borne in mind that, as stated in 15 *Corpus Juris*, page 1390:

> "If complainant's demand is of a purely equitable nature, recognizable only by a court of equity, he need not first establish it in an independent suit, but may do so in the creditor's suit to reach the equitable assets of the debtor."

In *Sill* v. *Kentucky Coal & Timber Development Company*, 11 Del. Ch., 93—the only Delaware decision cited on this subject in the opinions below—the allegations of the bill that the complainant was a creditor of the company were expressly admitted in the original answer of the defendant company, and were not denied in the amended answer; but the claim was made that because the complainant was not a judgment creditor he was not entitled to ask for a receiver. The Chancellor merely held "that it is not necessary that the complainant be a judgment creditor." No demand for a jury trial was made, and the constitutional question was not raised. Indeed, since the plaintiff's status as a creditor was admitted, there was no issue on that score to try. As said in 15 *Corpus Juris*, page 1390, on the authority of *Scott* v. *Neely*, 130 U. S., 106, and other Federal cases, "the admission or acknowledgment of the debt is equiva-

lent, for the purposes of the creditor's bill, to its establishment by a judgment."

The general rule that a Federal court is bound by the construction given a state statute by the state courts has the important qualifications that neither decisions of inferior state courts nor mere *dicta* of the state courts of last resort are controlling. The Federal courts are not bound to follow a construction of a state statute "based upon mere implication from the language of a judicial opinion" of a state court. (25 *Corpus Juris*, p. 811.)

Under these circumstances, we respectfully submit that the Delaware statute, even if constitutional and applicable in a Federal court of equity, has been wholly misconstrued by the courts below; and that it should be construed by this Court as in no wise subverting the defendant's right to a common law trial of a common law issue as to its liability on these notes.

FOURTH POINT.

The bill of complaint prays for no final relief whatever with respect to Hanssen's alleged rights as a creditor. The Federal Court, therefore, was without jurisdiction to appoint receivers for the assumed protection of his rights as a creditor; and any interpretation of the Delaware Statute which would authorize it to appoint receivers on such a bill and for such a purpose would clearly work an enlargement of the jurisdiction of the Federal Court and hence not be permissible.

The bill prays three kinds of relief: (1) for the appointment of temporary receivers; (2) for a decree directing the Pusey & Jones Company to execute and deliver to Hanssen a certificate for the shares of stock pledged by Christoffer Hannevig with Hanssen's principals; and (3) for a direction to the receivers to take steps immediately to have vacated and set aside the judgment in favor of the Baltimore Dry Docks & Shipbuilding Company, alleged to have been collusively suffered by the Pusey & Jones Company.

It is apparent upon mere inspection of the bill that *no final relief whatsoever is prayed for with respect to Hanssen's alleged rights as a creditor.* There is no prayer for judgment upon the alleged claim. There is no demand that the claim be impressed upon the Company's property as a lien, or that its property be sold to provide means of payment.

The prayer for a decree that the Pusey & Jones Company execute and deliver to Hanssen certain stock certificates has nothing to do with the satis-

faction of Hanssen's claim as a creditor or with the ground of jurisdiction on which the courts below have predicated their decree. Moreover, the suit purports to be a representative suit brought on behalf of all creditors and stockholders similarly situated (Rec., p. 6), whereas this prayer is entirely foreign to a representative suit and looks to an individual right which Hanssen asserts against the Company, not for its dissolution or liquidation but for recognition of his personal status as a stockholder. Furthermore, this prayer is not a prayer for any final relief to which any receivership is proper ancillary relief or necessary. If the Company has unlawfully refused to issue to Hanssen a certificate of stock, he has a perfectly adequate remedy; and no receiver is necessary to aid him in that regard.

So, likewise, as to the prayer that the receivers be instructed to commence suit to set aside the judgment obtained by the Baltimore Dry Docks Company. That is not a prayer for any final relief. It runs merely to an incident of the receivership. It does not ask that the alleged collusory judgment be nullified.

That such a bill does not confer jurisdiction upon a court of equity to appoint receivers is too clear for serious question. This for three reasons:

(1) The appointment of a receiver, in the absence of consent, is merely auxiliary and never the ultimate object of a suit in equity.

(2) Such an appointment can be made only in a pending suit in which the main relief is independent of the receivership.

(3) The pending suit must be one for such relief as could be litigated between the parties even if the application for a receivership were denied.

Courts and text writers agree that the remedy of receivership

> "is a provisional or auxiliary one, invoked as an adjunct or aid of the principal relief sought by the action *and never as the ultimate object of that action.* The court must have jurisdiction independent of the receivership and a receiver is never appointed except as a measure in aid of the enforcement of some recognized equitable right." (High on Receivers, 4th Ed., p. 10, §6.)

To the same effect are:

> 4 *Pomeroy's Eq. Jur.* (4th Ed.), p. 3375, Sec. 1423; and p. 3513, Sec. 1492;
> 1 *Tardy's Smith on Receivers* (2nd Ed.), p. 17, Sec. 4.

In *Tardy's Smith* (p. 51, §11) there is this statement:

> "The pending action must be one for such relief as can be litigated between the parties even if the application for the appointment be denied. Hence if the sole object of the suit is the appointment of a receiver, the court will not take jurisdiction in the absence of statutory provisions allowing such suits."

Uncommonly in point is *Zuber* v. *Micmac Gold Mining Co.*, 180 Fed., 625. There the bill alleged gross mismanagement of the defendant corporation, and asked that receivers be appointed to manage its property and to bring suit against another mining company, its officers and stockholders, for the purpose of recovering fraudulently issued stock. It prayed an injunction against the Micmac Gold Mining Company from transacting any further business. The bill did not pray for a cancellation of the contract alleged to be fraudulent,

nor for the winding up of the corporation. The Court held (p. 627):

> "In the case at bar there is no final relief asked for in the bill. *A receivership cannot be held by this court to be final relief; and it cannot be made final by the suggestion that the receivers may bring suits, and in that way obtain some ultimate relief.* The purpose of a receivership in equity is to be ancillary to, and in aid of, the primary object of the litigation. It cannot be the primary object of the litigation. The final relief sought by the bill cannot be made contingent upon the incidental relief of a receivership."

Important additional authorities are:

Brietson Mfg. Co. v. *Close*, 280 Fed. (C. C. A., 8th Cir.), 297;

De Rees v. *Costaguta*, 275 Fed. (C. C. A., 2nd Cir.), 172, 175; appeal dismissed, 254 U. S., 166;

Hutchinson v. *American Palace Car Co.*, 104 Fed., 182, 185;

Gutterson & Gould v. *Lebanon Iron & Steel Co.*, 151 Fed., 72;

In re Brant, 96 Fed., 257;

Robinson v. *W. Va. Loan Co.*, 90 Fed., 770;

McLean v. *Lafayette Bank*, 16 Fed. Cas. No. 8887.

In *Norris* v. *New York, N. H. & H. R. R. Co.* (a decision by Circuit Judge Manton, rendered May 23, 1919, and apparently not reported), Judge Manton said:

> "The purpose of a receivership in equity is ancillary to or in aid of the primary object of the litigation. The appointment of a receiver cannot be the primary object of the litigation, and so the final relief sought by a

> bill in equity cannot be made contingent upon the incidental relief of a receivership."

The prayer that the receivers be directed to bring suit does not give the Court jurisdiction.

As a matter of fact, the order below did not even *direct* the receivers to do anything. It merely (Record, p. 80):

> "authorized and empowered to take such action or proceedings * * * as they may deem proper or as they may be advised."

Peculiarly in point, therefore, is the ruling in *Zuber* v. *Micmac Gold Mining Co.*, 180 Fed., 625, that a receivership is not final relief (p. 627):

> "and it cannot be made final by the suggestion that the receivers may bring suits, and in that way obtain some ultimate relief."

To the same effect are:

> *Clark* v. *National Linseed Co.*, 105 Fed. (C. C. A., 7th Cir.), 787, 794;
>
> *Adler* v. *Seaman*, 266 *Fed.* (C. C. A., 8th Cir.), 828, 839;
>
> *Hutchinson* v. *American Palace Car Co.*, 104 Fed., 182;
>
> *Burnes* v. *City of Atchison*, 48 Kans., 507.

In the so-called "railway cases" the bill was brought by a lien or judgment creditor, or the plaintiff's status as a creditor was admitted. Generally, in *omnibus* suits, the decree rests on the fact that it was consented to.

Of course a state statute cannot so enlarge the jurisdiction of a Federal court in equity as to empower it to entertain a bill looking to the mere appointment of a receiver, unless in addition a special ground of equitable cognizance exists. *Alderson* v. *Dole*, 71 Fed. (C. C. A., 1st Cir.), 29, citing *Van Norden* v. *Morton*, 99 U. S., 378, and *Wehrman* v. *Conklin*, 155 U. S., 314.

FIFTH POINT.

As to Hanssen's claim to be a creditor, the only question now relevant is whether the courts below were right in holding that the issues involved in this claim must, over the defendant's protest, be tried by the Federal court in equity.

But, in any event, Hanssen clearly did not sustain the burden of proving that he was a creditor of the company. The contrary appeared.

I.

In order to reverse the decision below, it is not necessary now to prove that Hanssen was not a creditor of the company. It is enough to show that the courts below were wrong in their determination that that issue should ultimately be tried and adjudicated, over the company's protest, by the Federal court in equity, *i. e.*, that that court had jurisdiction.

The courts below have not *thus far tried*, or entered judgment upon, the issues as to the defendant's liability upon the notes. The ruling thus far is made solely on affidavits and is merely (in the words of Judge Morris)

> "that the complainant will probably be able to establish at final hearing that he is a creditor of the respondent company" (Rec., p. 523).

The defendant's answer expressly denies that Hanssen is a creditor "in any sum or amount whatsoever"; denies that he is the owner of the notes; denies that there is any sum due upon them; denies the evidentiary matter set up in the bill to

show that Hanssen is a creditor; and denies each and all of the claims and equities asserted by Hanssen (Rec., p. 140, *et seq.*).

Various claims of the company against Hannevig, the assignor of the notes, which claims were due and payable before the delivery of the notes to Hanssen's custody and exceed the amount of the notes, were pleaded as offsets; and the answer further set forth by way of defense that the notes were held by Hannevig and transferred by him to Hanssen's custody only after maturity and only for purposes of collateral security (Rec., pp. 140, *et seq.*).

These denials, allegations and offsets raise issues which can finally be determined in due course of law by judgment after trial, and as to which, we claim, the company was entitled to a common law trial (Rec., pp. 147-8).

II.

But Hanssen has not sustained the burden of showing satisfactory probability for his claim to be a creditor. Much less has he proved that he is one.

In order to establish that Hanssen was a creditor of the corporation, he was bound to prove (1) that he was personally entitled to sue on the notes which he held; (2) that the notes were then due and payable, and (3) that the company had no valid defense to the payment thereof.

Hanssen failed to sustain the burden of proof on any one of these points.

On the first point, the notes were deposited by Hannevig with Hanssen under the same contract conditions as the deposit of the stock, and he had no more title to them than he had to the stock.

(See the circumstances stated in the next Point, p. 53.)

These notes were eight in number, all drawn to the order of Christoffer Hannevig, Inc., and signed by the Pusey & Jones Company, with one exception where the note was drawn to the order of Christoffer Hannevig. They were all indorsed on the back with the following notation (Rec., pp. 34-41):

> "Extended according to letter dated September 18, 1917, to United States Shipping Board Emergency Fleet Corporation."

This notation in each case was signed by the payee of the note. They were then again indorsed with the signature of the payee (Rec., pp. 33-41). The terms of this agreement of postponement were assented to by Hannevig and by Hannevig, Inc. (Rec., pp. 103, 116-7).

We need not repeat the argument, which is set forth in the next Point (p. 53) in connection with the stock certificates, showing that complainant was at best a mere custodian of these notes under the agreement of February 13, 1920 (Rec., p. 189). Nor need we again repeat the arguments in that Point to the effect that there was no authority conferred upon Hanssen in the power of attorney which he held to hold these notes as pledgee or to bring suit on them against the corporation (Rec., p. 495). He was a mere custodian of the notes as things held in possession. He was authorized to make them a part of his negotiations, but he was in no way authorized to bring suit upon them against a third party to the transaction.

In point of fact, it is obvious that under the terms of the paper under which the notes were

delivered to Karluf Hanssen (Rec., p. 489), no suit whatever could be brought upon them by any party exercising rights under the terms of that paper. The paper provided that Christoffer Hannevig reserved to himself the right that "the deposited security," which included the notes, should be delivered to him and could be disposed of by him at any time, provided he paid his obligations to the nine ship-contract owners in certain kinds of currency. This reservation took away from the Norwegian ship-contract owners, not to mention Karluf Hanssen, any right at all to sue upon the notes, or to endeavor to collect the same as if they were the holders of this negotiable paper. They merely held this paper. It was impossible for Hannevig to negotiate it or sell it without a payment satisfactory to them of the indebtedness which he owed them; but they themselves were not authorized to negotiate the paper or collect upon it.

Karluf Hanssen's position was, of course, still further removed from any rights in these instruments, since he was merely holding this paper as a custodian for the nine ship-contract owners. He, therefore, could have no status as a creditor, even if the paper were then due and payable, and even if there had been no defense to the notes which the Pusey and Jones Company could properly set up.

The Courts below held that the endorsement of a note to an agent transfers to him title thereto as against all parties except his principal.

As to the latter point, we are of opinion that when a note endorsed in blank is delivered along with a collateral instrument specifying that it is delivered merely as collateral to the claim of a third

party, the mere manual recipient does not acquire title. The written instrument controls the character of the manual delivery. Manual delivery to the individual is only effective to transfer title to him when so intended; and when the intention is not to transfer the title to him, but to give security to third parties and this is stated in a collateral instrument handed over at the same time, the manual recipient does not acquire any title by the delivery.

III.

There is a still further objection which it is submitted is decisive on this point. Before the transfer of the notes, they were endorsed with a modification of maturity which referred to the terms of an outside instrument; and the invariable rule is that such an endorsement deprives the paper of negotiability. This endorsement referred to a letter written September 18, 1917, to the effect that the due date of the notes should be extended until the completion of the last eight ships then under process of construction in the Wilmington yard. The last ship of the vessels specified was actually completed about the first day of August, 1919 (Rec., p. 369). Therefore, when the notes were turned over to the custody of the complainant in February of 1920, they were overdue, and in addition, were non-negotiable, since their terms were modified by an outside agreement existing between the parties.

But though these notes were overdue, collection thereof had been postponed by an express agreement between the parties. This agreement postponed payment of the $650,000 in notes until the

entire amount of the mortgage loan made by the United States Shipping Board Emergency Fleet Corporation and the Pusey & Jones Company had been paid, together with interest thereon. This is the provision set forth in Paragraph 22 of the agreement made May 14, 1918, between the Shipping Board and the Pusey & Jones Company (Rec., p. 228). This extension of collection was assented to in writing by Christoffer Hannevig, Inc., and Christoffer Hannevig, the payees and holder of the notes at that time (Rec., pp. 403-5).

There was no dispute of the above facts. Hence it is demonstrated Hanssen had acquired possession of these notes as overdue paper. He could, therefore, under no circumstances, be regarded as a creditor of the Pusey & Jones Company. He could not sue as a creditor of the company until he was entitled to demand payment of the notes; and at that date the company might be well able to pay him, and his position as a creditor would then have vanished.

There is no rule which permits merely *a prospective, common-law creditor* to present a creditor's bill and secure a receiver when his debt is not payable and may be paid and cancelled before it became collectible at law.

That Karluf Hanssen had full knowledge of this postponement of the payability of the notes, is manifest from the facts set forth in the affidavit of James B. Simpson (Rec., p. 448, *et seq.*). But his knowledge would be immaterial, since he took the paper after maturity and consequently was bound by all the equities which existed between the original parties thereto.

IV.

Furthermore, the Pusey & Jones Company had an off-set against these notes in the hands of Hanssen as assignee of Hannevig, which off-set exceeded the amount of the notes. Hanssen, therefore, was not a creditor.

On February 11th, 1920, the Baltimore Dry Docks & Shipbuilding Company deposited $750,000 with Hannevig as President of the Pusey & Jones Company as earnest money on its purchase of the latter's Gloucester plant. Hannevig immediately deposited the money in his private banking house and appropriated it to his own uses (Rec., pp. 375, 412). Thereafter, the Pusey & Jones Company was unable to comply with the contract of purchase, and the Baltimore Dry Docks Company recovered judgment against it for the $750,000 deposited, with interest.

This $750,000 never reached the treasury of the Pusey & Jones Company; and from February 11, 1920, that Company had a cause of action against Hannevig for its misappropriation. This cause of action antedated the agreement of February 13, 1920, under which Hannevig delivered the notes to Hanssen (Rec., pp. 485, 489).

Had Hannevig sued on the notes, the cause of action for the misappropriation above described would have been a valid set-off. Does Hanssen stand in a better position?

We claim that Hanssen took the notes subject to to the equitable defenses which the Pusey & Jones Company could have asserted against Hannevig; and that these defenses operated to overbalance the claim upon the notes. This is true, we claim, for a number of reasons.

(1) The contract between Hannevig and Hanssen was made in New York (Rec., pp. 485, 489); and under the New York statute and decisions such an off-set against the assignor is also available against an assignee not a holder for value, without notice and in due course. Hence Hanssen took the paper subject to such defenses thereto as were allowed by the law of New York.

The rights and obligations of the parties to a transfer of negotiable paper are determined by the law of the place where the transfer is made (*Amstuck* v. *Rogers*, 189 N. Y., 252). Hence, in the present instance, the New York law must determine whether the transfer passed the notes free from set-offs or not.

Pritchard v. *Norton*, 106 U. S., 124, established that

> "whatever goes to the substance of the obligation and affects the rights of the parties, as growing out of the contract itself, or inhering in it or attaching to it, is governed by the law of the contract."

In this same opinion this Court adopted the rule laid down by *Story's Conflict of Laws*, Section 332:

> "If by the law of the place of a contract, equitable defenses are allowed in favor of the maker of a negotiable note, any subsequent endorsement will not change his rights in regard to the holder. The latter must take it *cum onere*. *Evans* v. *Gray*, 12 Mart. (La.), 475; *Ory* v. *Winter*, 4 Mart. n. s. (La.), 277; *Charters* v. *Cairnes*, *id.*, 1."

In *Northwestern Mutual Life Insurance Company* v. *McCue*, 223 U. S., 234, it was held (p. 246):

> "The obligation of a contract undoubtedly

depends upon the law under which it is made."

Directly in point is *Creston National Bank* v. *Salmon*, 117 Mo. App., 506, which followed and adopted the principle laid down in *Pritchard* v. *Norton, supra*. The contention there advanced was that matter of defense guaranteed by the *lex loci contractus* ran to the remedy rather than to the nature of the obligation and that therefore the *lex fori* was controlling; but the court held otherwise and followed *Pritchard* v. *Norton*, saying (p. 513):

> "Where the statute where the contract is made and to be performed operates to extinguish the contract or debt itself, the case no longer falls within the law in respect to the remedy, and when such a contract is sued upon in another state, the *lex loci contractus* and not the *lex fori* is to govern."

The situation with respect to the Pusey & Jones notes is directly covered by this doctrine.

Section 267 of the Civil Practice Act of New York (formerly Sec. 502 of the Code of Civil Procedure) provides:

> "If the action is upon a negotiable promissory note or bill of exchange which has been assigned to the plaintiff after it became due, a demand existing against a person who assigned or transferred it after it became due *must* be allowed as a counterclaim to the amount of the plaintiff's demand if it might have been so allowed against the assignor while the note or bill belonged to him."

The mandate of this statute has always been observed by the state courts.

Woods v. *Sizer*, 102 Misc. (N. Y.), 453 455;

Hunter v. *Fiss*, 92 App. Div., 164;
Czerney v. *Haas*, 144 App. Div., 430;
Tierney v. *The Peerless Shoe Co.*, 33 Misc., 803, 804;
Roldan v. *Power*, 14 Misc., 480.

The court below refused to apply the New York rule on the ground (Rec., p. 649) that it was "an exception" to the general rule which permitted as offsets merely such equities or defenses as attached to the paper itself. But the New York rule is none the less controlling as the law of the place of the contract.

(2) Even the application of the technical common law rule that only claims existing against the paper itself may be set off against the transferee of overdue negotiable paper, is hedged about with limitations which the courts below failed to appreciate and apply.

Only in the hands of one who takes the commercial paper after maturity *as the absolute owner for value* do the defenses against the prior holder fail to attach under the technical common law rule. Where, however, the commercial paper is assigned as collateral, as in this case, even those jurisdictions which apply the technical doctrine recognize that claims against the assignor are valid defenses in a suit upon paper in the hands of a pledgee.

Janness v. *Bean*, 10 N. H., 656.

Surely a mere pledgee can stand in no better position than his pledgor. He is suing for the benefit not only of himself but of the pledgor; and the pledgor is the beneficial owner of the proceeds of the suit subject only to the pledge.

(3) Furthermore, the complainant is asserting his alleged rights in a court of equity. The aforesaid technical rule against set-offs grew out of the niceties of common law pleading. It never obtained in equity where the principle of off-set in such cases has always been recognized. By suing in equity Hanssen has waived the technical common law rule. Particularly in cases where the assignor of overdue negotiable paper is insolvent, equity will take cognizance of claims which might have been asserted against the assignor. The Pusey & Jones Company is especially entitled to the protection of courts of equity against any claimant who holds under the bankrupt Hannevig and asserts the insolvency of the Pusey & Jones Company as a result of the judgment which has been taken against it by the Baltimore Dry Docks Company as a consequence of Hannevig's misappropriation of the $750,000 payment involved in that transaction.

Defenses existing against the person of an insolvent assignor were allowed by this Court in *Rolling Mill* v. *Ore & Steel Co.*, 152 U. S., 596. This Court held (p. 616):

> "By the decided weight of authority it is settled that the insolvency of the party against whom the set off is claimed is a sufficient ground for equitable interference."

In New York, courts of equity have long held to this doctrine. In *Davidson* v. *Alfaro*, 80 N. Y., 660, the New York Court of Appeals held, in a *per curiam* adoption of the decision below, page 662:

> "It is a rule in equity, on bill filed therefor, that cross-demands, though unliquidated by judgment, will be set off against each other and if, from the situation of the parties, justice

cannot otherwise be done; and the insolvency of one of the parties is a sufficient ground for the allowance of a set off in equity, even if not within the statute of set offs."

To the same effect are:

Leeds v. *Marine Ins. Co.*, 6 Wheat, 565;
Lindsey v. *Jackson*, 2 Paige, 581;
Smith v. *Felton*, 43 N. Y., 419;
Dubreuil v. *Gaither*, 98 Me., 541;
Garner v. *Price*, 4 Kulp., 10;
Blake v. *Langdon*, 19 Vt., 485;
Hobbs v. *Duff*, 23 Cal., 596.

SIXTH POINT.

The plaintiff's alleged status as a stockholder has not been considered in the courts below to be, and is not, sufficient ground of jurisdiction. Consequently, the question as to his status as a stockholder is not here as a question of law for determination.

(1) In the District Court Judge Morris said of Hanssen's claim to be a stockholder (Rec., p. 521):

> "It appearing that the complainant is a creditor who may maintain this suit in this court is is unnecessary now to determine whether he is also a stockholder as alleged."

Hence, there is nothing to indicate that if jurisdiction had rested on Hanssen's status as a stockholder, the District Court would have exercised its discretion in favor of appointing receivers. In that event very different considerations of policy and expediency would have been invoked.

The same view of the matter was taken in the Circuit Court of Appeals (Rec., p. 650).

Consequently, Hanssen's disputed claim to status as a stockholder presents no question for determination in this court which is only concerned with the questions of law raised by the jurisdiction actually exercised.

(2) Moreover, as a mere custodian of Hannevig's stock certificates on behalf of the pledgees of the certificates, Hanssen was not a stockholder of the Pusey & Jones Company within the meaning of the Delaware statute.

Hanssen was never a stockholder of record of the Pusey & Jones Company.

Hence, upon his claim as a stockholder seeking to invoke the Delaware statute, Hanssen is in no better position to secure the relief he asks in the Federal court than he is upon his claim to be a simple contract creditor. He has failed to reduce his status to ownership of record, just as he has failed to reduce his contract debt to a judgment. In either case, he has but a cause of action.

The Delaware statute clearly does not contemplate an extension of the Chancellor's jurisdiction to anyone who merely asserts an interest in a certificate of stock. The applicant must be an actual "stockholder" at the time of making the application. The statute is astonishingly drastic and arbitrary, and will receive only the strictest construction.

(3) Furthermore, the power of attorney under which Hanssen held the stock certificates did not authorize him in any way to maintain any action thereon and did not constitute him personally a pledgee of the stock. Nine Norwegian parties (individuals and corporations) had been induced by Hannevig through false representations to pur-

chase rights in certain contracts (Rec., p. 439, *et seq.*). When the fraud was discovered, these nine parties employed Hanssen, who was an attorney at law, to take steps to enforce their rights and gave him a power of attorney, the material part of which reads (Rec., p. 495):

> "We, the undersigned, members of 'the Christiania Group of Norwegian Shipowners,' hereby authorize Mr. H. Karluf Hanssen, attorney at law, of Haugesund, to negotiate on our behalf, and in case, to make a binding agreement with Mr. Christoffer Hannevig regarding payment of security, thereunder, in case, payment in the form of tonnage, for all 'overpayments' and differences in instalments pertaining to the nine contracts belonging to us at the Pusey and Jones yards and, in case, to take all legal steps which he may deem necessary in order to secure our said claims."

No one of these powers gave Hanssen authority to hold, either as the owner of the stock or as a pledgee thereof, any stock or securities given to him by Christoffer Hannevig, nor did the power of attorney authorize Hanssen in any way to maintain any action whatever on such stock. He was given no right to sue in his own name—much less to bring an action as a stockholder to have a receiver appointed for any corporation. Any legal steps which Hanssen was authorized to take were legal steps aganist Hannevig and not against the Pusey & Jones Company.

Under this power of attorney, Hanssen negotiated with Hannevig on February 13th, 1920, the agreement set forth in Hanssen's rebuttal affidavit (Rec., p. 489). By that agreement, Hannevig acknowledged the delivery to Hanssen, as representative of the nine Norwegian parties, of certain

securities "given below as security for correct payments for obligations with interest which are now due." The instrument then reserves to Hannevig the following right (Rec., p. 489):

> "*I reserved that the deposited values* (i. e., the stocks and notes) *shall be delivered to me and can be disposed of by me free of any encumbrances on condition that I pay my obligations in Norwegian currency at an exchange taken at the respective instalment dates* with an interest of 6 per cent., and this shall not acknowledge that I am bound to pay anything else, except $565,875.00, which I have already paid out in taking over the S. S. 'Fire Island,' in American Dollars."

Obviously this paper was not sufficient to make Hanssen personally a pledgee or owner of any of the securities delivered. The securities were merely delivered to him as custodian. He became a depositary and nothing more. *A fortiori* he did not become a stockholder.

The contract of delivery contains no provision that the persons to whom the stock is delivered have any right of sale over it. That right is reserved expressly to Hannevig. All that the nine Norwegian parties could do was to hold the stock and notes until ultimately paid by Hannevig, or possibly they could bring a suit against Hannevig to foreclose their lien.

No notation of the pledge was ever made upon the stock books of the corporation, as is required by the Delaware statute. The General Corporation Law of the State of Delaware provides:

> "Whenever any transfers of shares shall be made for collateral security, and not absolutely, it shall be so expressed in the entry of the transfer" (Sec. 16).

> "Persons holding stock in a fiduciary capacity shall be entitled to vote the shares so held, and persons whose stock is pledged shall be entitled to vote, unless in the transfer by the pledgor on the books of the corporation he shall have expressly empowered the pledgee to vote thereon, in which case only the pledgee, or his proxy may represent said stock and vote thereon" (Sec. 18).

There is nothing in the agreement with Hannevig of February 13th, 1920, if it can be regarded as a pledge at all, giving the pledgee the right to vote the stock (Rec., p. 189); and no request was ever made upon the company for a notation on the records that the transfer was made for collateral security. The demand made in this suit for a transfer to Hanssen is a demand for an absolute transfer and not a transfer in accordance with the Delaware statute, indicating that Hanssen would hold the stock as collateral security (Rec., p. 23). There is nothing to show that the pledge has ever been foreclosed.

All the statements which appear in the affidavits or answer filed on behalf of the Pusey & Jones Company, describing Hanssen as a pledgee of stock, refer merely to his technical rights in that respect as disclosed by the information then in possession of the company. The subsequent disclosure of his real relationship, as set forth in the power of attorney filed with his affidavit of rebuttal, and in the authentic copy of his agreement with Hannevig, deprives him of any status whatever as either owner or pledgee of the stock, and supersedes those statements.

(4) Even had Hanssen a status as pledgee, it is submitted that he would have no right to main-

tain this bill as a "stockholder" under the Delaware statute.

No decision is or can be cited that a mere pledgee is a stockholder within the meaning of that statute. The dictum of Judge Goff in *Gorman-Wright Co.* v. *Wright*, 134 Fed., 364, refers only to the general power of a pledgee of stock "to be heard in a court of equity concerning its preservation and the protection of his interest therein."

That dictum has no reference to the Delaware statute. It is based on a section of Judge Thompson's work on corporations which has been omitted from the later editions thereof; on a reference to Kent, which is clearly erroneous; and on the text of 22 A. & E. Ency. of Law 907, which is supported by a single citation (*Baldwin* v. *Canfield*, 26 Minn., 43). That single citation is a square authority against Hanssen because it holds that, whereas the equitable owner of stock might under the peculiar circumstances of that case bring a suit in equity to remove a cloud on the title of the corporate property, he could not do that directly as a *stockholder*.

Wherever relief has been afforded in equity to the pledgee of stock, it has been because of his property interest, not because he was a stockholder.

In Elyea *v.* Lehigh Salt Mining Co., 169 N. Y., 29, and Pray *v.* Todd, 71 N. Y. App. Div., 391, it was held that, under statutes as to a pledgee's rights similar to the Delaware statutes quoted above, a pledgee of stock which remains standing in the name of the pledgor on the books of the company has no voice in the affairs of the corporation.

SEVENTH POINT.

The Pusey & Jones Company was greatly aggrieved and irreparably damaged by the jurisdiction assumed and the decrees made below.

The grievance of the Pusey & Jones Company is that, without jurisdiction or due process of law, it has been deprived of the control of its own affairs. At a time when the Company's difficulties were being ironed out without any waste or threat of waste of its assets, and without any threat of piecemeal sales thereof, the Court appointed receivers for the corporation *ex parte*, being of the opinion that the Company was insolvent. The District Court seems to have been largely influenced in the exercise of its discretion by the fact that a large judgment had been obtained against petitioner by Baltimore Dry Docks & Shipbuilding Company, and by the charge that this judgment was collusive. But execution on this judgment had been, by agreement, adjourned for many months (Rec., pp. 379, 398).

The Company had no current obligations which it was not able to meet out of the funds in its possession, which included $190,000 cash on hand and $240,000 in immediately negotiable paper (Rec., pp. 364-366). The Company was successfully conducting its affairs and was able to continue to do so (Rec., pp. 150, 151, 345-346, 371, 363-365). Substantially all important stock and creditor interests (except Hanssen) had entered into an agreement (Rec., p. 65), through the operation of which it was expected that the Company would continue to carry on as a going concern pending the adjustment of its large claim of approximately $14,000,000 against the Shipping Board, the settlement of which was

expected to take care of the Baltimore Dry Docks Company's judgment, and leave the Pusey & Jones Company a cash balance over all liabilities of several million dollars (Rec., pp. 157-158, 345-417). This agreement would certainly not have been entered into had not the parties thereto believed that the settlement of the large claim against the Shipping Board would result in making the stock of the Pusey & Jones Company of considerable value.

CONCLUSION.

The decrees below should be reversed; the bill of complaint dismissed, and the receivership vacated, with costs.

Dated, New York, February 5th, 1923.

Respectfully submitted,

LINDLEY M. GARRISON,
CHARLES H. TUTTLE,
SELDEN BACON,
SAUL S. MYERS,
Of Counsel.